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EXPLORATIONS IN SOCIAL ECONOMICS

Revisiting the Relevance of International Trade Theory

Mark A. Lutz

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Abstract Probably one of the most controversial contributions to the literature of international trade theory was offered by the late social economist John Culbertson. In his view, low wage competition among corporations in a world characterized by capital mobility and massive trade deficits undermines the foundation trade theory based on David Ricardo's celebrated notion of comparative advantage. Instead, there are several good reasons to believe that international trade with China, India, Vietnam, etc. will be governed by absolute advantage. The current essay is dedicated to the virtually ignored work of Culbertson, and it is meant as an invitation for social economists to critically evaluate the argument and in the process make an attempt to point out where it goes wrong.

Keywords Comparative advantage · Low wage competition · Outsourcing · John Culbertson · Absolute advantage

There are few matters that most economists can agree on, but one is the long-held conviction that the free flow of goods, services, and capital across international borders, a flow uninhibited by tariffs and other obstructions, will benefit all the trading partners. Thanks to David Ricardo's insight regarding comparative advantage, the almost three-century-old predilection toward "laissez aller, laissez

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M. A. Lutz (✉)
School of Economics, University of Maine, 153 North Chester Dean Road,
Lincolnville, ME 04849, USA
e-mail: marklutz@tidewater.net

faire" was early on extended to foreign trade, and remains the gospel in today's modern global world.

In sharp contrast, economists of the humanistic tradition have long been skeptical of the 18th-century "natural harmony" doctrine that underlies so much of economic theory. Instead of relying solely on some "invisible hand" directing economic affairs, humanistic economists since Sismondi's *New Political Economy* (1819) have recognized the necessity of appealing to government regulation to bring about the common good.[1] Among other issues, Sismondi spent a chapter of his book discussing the real costs and benefits of the British Corn Laws. He opposed Ricardo because he feared that the low-cost (serf-produced) corn imported from Eastern Europe would do much to destroy English farming and create unemployment, thereby also weakening purchasing power and effective demand for British manufactured goods (Sismondi 1991, pp 204–205). More generally, Sismondi was a pioneer in basing government policy on institutional realities and empirical facts, rather than abstract reasoning of the type professed by Ricardo and indulged in by orthodox economists to this day.

In this essay, I want to bring attention to the work of the late institutionalist economist John Culbertson. During the 1980s, in good humanistic style, he boldly threw himself against the mainstream, only to suffer the fate of so many who dare to think "outside the box": the fate of being ignored rather than rebutted. Looking at Culbertson's contribution to trade theory some 20 years later, a rather strong case can be made that he might have gotten it right, both theoretically and empirically. I believe the time has come to remind social economists of Culbertson's basic argument and challenge, and to invite an open-minded assessment and critical discussion.

John M. Culbertson as a Maverick Social Economist

Originally, Culbertson devoted his time as a professor at the University of Wisconsin to development and monetary issues.[2] He started writing about trade in 1974, but after having little luck finding proper outlets for various unpublished manuscripts, he created the 21st Century Press in order to self-publish his work. In 1984, *International Trade and the Future of the West*, meant as a challenge to the profession, arrived in print. In the preface he writes: "I hope that economists will resist the natural inclination to reject out of hand this challenge to their traditional doctrines, and will make reading this book the occasion for a basic rethinking of the subject, of the taken-for-granted assumptions on which the conclusions of orthodox economic theory depend, and of the proper relation of economics to present-day empirical science and its view of the world" (Culbertson 1984, x). Even though he promoted it heavily by mailing flyers, it did not take long for him to realize that his hope was misplaced.

[1] See, for example, Lutz 1999, ch.1.

[2] Among other positions, he was an economist with the Board of Governors of the Federal Reserve System, the Subcommittee on International Finance of the House Banking and Currency Committee, and the United States Agency for International Development Mission to Bolivia.

Perhaps in response to what might be called total neglect, he repeated his case in a booklet published a year later, *The Dangers of "Free Trade"* (1985). As a result of promotion by trade unionists, the popular media—including, among others, the *New York Times,* the *Los Angeles Times*, and a front-page article in the *Wall Street Journal*—soon reacted and thereby helped spread his basic message.[3] Economists, when pressed, made short shrift of the matter. According to the *Wall Street Journal* article, Robert Lawrence from the Brookings Institution labeled it a "flat-earth theory," while Paul Krugman (1996) frustratedly chose to liken the publicity given to Culbertson's heterodoxy to a situation of "someone talking about the psychic power of plants getting the same attention as people doing research on recombinant DNA." All the media attention evoked "considerable hand-wringing among the Wisconsin economics faculty." The article continued that "Eugene Smolensky, the department chairman, [said] a mood of 'doom and gloom' [pervaded] the department" every time Culbertson appeared in the *New York Times*.[4]Among the faculty, serious discussion of the subject was taboo. Professor J.D. Richardson, the department's trade specialist, confided to the *Wall Street Journal* "that he and Mr. Culbertson usually talk about subjects like weather and scrupulously avoid the topic; 'it's like those issues in a family that you promise never to bring up again,' Mr. Richardson explained."

Methodologically, the circumstance that scientists are unable to overcome the natural inclination to reject out-of-hand a serious paradigmatic challenge, that they tend to react with uncomfortable silence rather than responding with an open mind, is nothing terribly new, but nevertheless disturbing and quite unacceptable. It is one thing to avoid talking about deeply controversial, perhaps even embarrassing, matters en famille or within an academic department. But, as we shall see, Culbertson did not fare any better at the hands of the profession at large.

Against the background of mounting trade deficits with Japan, the talk of a North American Trade Agreement with Mexico, as well the prospect of the imminent entry of China into global manufacturing,[5] Culbertson published all his trade-oriented concerns within a few years in the 1980s—a notable exception being a brief piece in the fall of 1991 in which he strongly opposed the "uniquely destructive human folly" of free trade with Mexico. Of all his publications, his first book (1984) makes the most comprehensive case; shorter and perhaps more readable versions repeating the basic argument followed (1985, 1986, 1987, 1989, 1991).[6] Unfortunately, John Culbertson was soon to be struck by a debilitating illness and had to take permanent leave of the academic scene. In what follows, I will attempt to faithfully render his basic argument and then briefly observe what happened in the following 20 years.

[3] *NY Times,* 27 March 1986 and 9 August 1986; *Los Angeles Times,* 18 February 1987; *Christian Science Monitor,* 15 June 1987; *Wall Street Journal,* 2 April 1987 (Blustein 1987).

[4] Blustein 1987: 1. We are also told that colleagues said Culbertson didn't appear to be motivated much by money; he earned relatively little—between $5,000 and $10,000—from his speeches. His salary, set by his peers, suffered in predictable fashion: during that period he made $45,000, just a bit more than half the pay received by the department's stars. Culbertson is reported to have remarked: "I'm not starving, but every year when the salary issue comes around, you feel like someone spit in your eye again."

[5] This was before the Tiananmen Square Crisis that came as a blow to reformers and did much to postpone China's massive entry into the world market by some half dozen years.

[6] From this point on, unattributed references will be to Culbertson's work.

Culbertson's Case against Conventional Trade Theory

In the mid-1980s, Culbertson (1984, p 35) lamented that "the recent literature and textbooks of economics have supported the free-trade doctrine." He blamed the early economics of the "invisible hand" with its underlying idea of "natural harmony" under "natural liberty" as professed by Adam Smith and further developed by others. Following this tradition, universal principles or laws are given preference over cause-and-effect explanations. Still today, theoretical economics provides models and theories that derive from a set of assumptions, which reflect more of a political faith or ideology than reality. In particular, to say that unregulated international trade is automatically beneficial because of some "principle of comparative advantage" is to offer a verbal formula in place of the causal processes, laws, and institutions that actually shape actions and events (Culbertson 1984, p 10). Such a stance appeared to him especially dangerous at a time when China, Indonesia, and India were poised to add some two billion workers to the global labor force, all occurring in a world made smaller by the ongoing revolutionary changes in transportation, communication and information technology. For these reasons, the purpose of Culbertson's (1984, pp 35, 5) first book, and all that followed, was "to contribute to the understanding of international trade within a realist or scientific economics" and "to devise policies that will make international trade in the troubled world of the late twentieth century a force for human betterment rather than…decline."

One of the realist types of evidence that sheds some light on the trade issue is the lesson of history. Additional real-world factors that need to be reckoned with include a better appreciation of the dark side of competition, as well as the importance of the nation state as protector of the welfare of its citizens. Let us take a quick look at each of these three elements.

Lessons from History: The Rise and Decline of Nations

Among the historical events illustrating the importance of trade patterns affecting the decline of nations, Culbertson made much of the 17th Century deindustrialization of northern Italy as reported by economic historian Carlo Cipolla. He attributed the decline of Italy's once prominent manufacturing to letting the market respond when faced with the strong new winds of British and Dutch competition.

> From the 11th to the 16th centuries, foreign trade had been indeed an "engine of growth" for Italy…. From the beginning of the 17th century, however… the structure of Italian foreign trade changed completely. Foreign manufacturers were brought in and drove Italian products and their manufacturers out of the market. At the same time foreign demand favored the production of oil, wine and raw silk. One may argue that in the short run Italy derived from this new arrangement some comparative advantages of the kind illustrated by the Ricardian theory. In the long run, however, foreign trade acted as an "engine of decline": it contributed to shift both capital and labor from the secondary and tertiary sectors to agriculture. In regard to labor this shift meant, in the long run, a) the reduction in number of both the literate craftsmen and the enterprising merchants, b) the growth in size of the illiterate peasantry, and c) the rise in

> power of the landed nobility…. The cities lost their previous vitality. The great Universities of Padua and Bologna slipped into oblivion. Venice sent her best gun founder, Alberghetti, to London to learn the most modern techniques for working metals. The few remaining Italian clock makers copied the style and the mechanisms of the numerous and skillful London clock makers. Italy had begun her career as an underdeveloped area within Europe. (Cipolla 1976, pp 242–44).

The story of Italy's decline, centering on a changing pattern of trade, can also be told about other countries.[7] Spain, for example, relied too much on the inflow of gold for its power, showed disdain for industry, and did nothing to provide for the nation's economic future, to develop its "productive power" as Friedrich List put it. It did not take long for it to become a backward nation. Conversely, England became an economic power, not because of laissez faire but by direct government actions like the prohibition of Spanish wool or the wearing of foreign cloth, and the support of shipping and the merchant marine. Similarly, it is well known that the United States economy grew to a dominant position in the decades following the Civil War because of a wall of tariffs protecting them from European competition (Culbertson 1989, pp 70–74). Today, government enhancing the productive power of its national economy by picking and protecting a desirable industry pattern has long been called "industrial policy."

Reckoning with the Dark Side of Competition

The mid-1980s was also the period when the deregulation movement began to sweep politics in the United States. Culbertson (1985b) did not share the general faith in the effectiveness of competition in coordinating economic transaction and allocating economic resources.[8] Instead, he was concerned that economists and politicians underestimated the dark side of competition. To this effect, he felt compelled to write and publish a little booklet titled: *Competition: Constructive and Destructive*. In any organized activity, we are told, there are two ways to be a winner: (1) give a superior performance within the existing framework of rules, or (2) avoid playing by the rules. Examples of the latter type of competition are the devious ways of saving costs by disregarding safety standards, falsifying inspections, bribing government officials, and doctoring balance sheets. In addition, skillful bending of rules includes the standard-lowering competition by local governments that aim to offer a better "business climate" (tax concessions, lax regulation, and so on) in order to attract industry. Internationally, such destructive competition translates into a beggar-thy-neighbor type lowering of labor and environmental standards. Such activity, obviously prevalent in the practice of international outsourcing, puts an unfair

[7] For a more comprehensive discussion, see Culbertson (1989, pp 48–55).

[8] Culbertson repeatedly denied any reality or relevance to the theoretical machinations of modern welfare economics. "The argument that 'the price system' and 'competition' bring about perfect allocation of resources, on examination, has no applicability to actual events." Instead, applicability was confined to an ideal world of idealized competition and prices making for "a wish-world, of the kind created by ideologies" (1989, p 91).

burden on the corporations at home who are obliged to play by a more stringent set of rules. The resulting pressure tends to undermine a country's power to set and properly enforce its own social standards. The market will not respect, nor permit, pockets of decent behavior in a world of unfair competition. Rather, good guys are condemned to finish last.

The Socio-Economic Importance of the Nation-State

An emphasis on social control by means of an active government managing the economy tends to go against the grain of economists, whether in academia or business. It does not fit well with the notion of economic man and the ideal of individual freedom and "free trade." Such dissonance, Culbertson (1984, p 33) reminds us, is deeply rooted in the history of the science, going back to Adam Smith: it is the creed of Nature supposedly having designed the world so that things work out best when each person does as he or she wishes. The human being, in this tradition of thought, when acting "with' really acts as "Nature's preprogrammed robot" for the good of humanity. As a result, government's intrusion would violate Nature's Plan as well as the "rights" Nature conferred on people to do as they wish. The less the state messed with the freedom of people and business, the better.

In stark contrast, Culbertson (1984, p 39), as a social economist, decried the excessive individualism pervading economics. To him, human beings exist first and foremost as social beings and develop in organized groups. People establish organizations to ensure that independent action by the parts will be in harmony with the interests of the whole. We are given the following illustration:

> [An] organization must designate a person or group as its agent, to act on behalf of the organization. It is understood that, say, a purchasing agent for Xerox Corporation is acting on behalf of the Corporation, not acting to make money for his own pocket. For the purchasing agent to seek his own profit, by taking a bribe to give Xerox's business to Firm Z, would be violating the trust imposed in him, violating the rules of Xerox Corporation, and likely breaking a state law as well. It would seem nonsensical to propose that any employee of Xerox—or even that anyone whatever—should be permitted to take action affecting the interests of the Corporation, for example, to make a decision as to what it should buy, and from whom, at what price. The organization can be effective, and survive, only if it has control over actions that affect its interests.

Extending the same logic to cross-border trade would imply that the nation, as the highest-level national government organization, must oversee the actions of its constituent parts to assure that they are in the public interest. What is good for General Motors is not necessarily good for the United States. Blank-check outsourcing of production to low-wage countries is not likely to be in the interest of the home country, whose government has the obligation to protect society's standards of worker protection, environmental integrity, product safety, etc., from being weakened.

Similarly, Culbertson decried the goal of a "world economy" as being the ultimate vision of utopian individualism ordained by Nature. Given mankind's propensity to belong to groups, tribes, and religious affiliations, an integrated global economy would not bring peace and universal brotherhood, but ethnic and cultural warfare instead.

Culbertson (1985, p 35) turned to evolutionary biology to find the roots of the propensity to band together in territorial arrangements. Among the higher animals, such behavior permits a constructive competition or selection among groups. The ones that permit overpopulation or destruction of their habitat and food supply will not survive, while the ones that limit population and protect their environment will thrive and become the pattern setter for the species. Internationally, it works the same: for humanity to progress we need nations that can achieve success through controlling their own affairs—only then are they in a position to help the poorer nations by means of sharing their markets, their technological achievements, and more generally, setting patterns that can be copied. It would, therefore, follow that "communalizing the nations through unregulated foreign trade would be, from an evolutionary perspective, catastrophic" (Culbertson 1989, p 103).

Underlying Myths of Trade Theory

As one would expect, trade theory, too, has been shaped by the thought of the founding fathers of economics. Unfortunately, time has not stood still, and, as we shall see, what was a reasonably accurate description of reality some 200 years ago may be much less so today. At the very heart of Culbertson's attack are a number of basic "intellectual confusions" or false beliefs clouding modern textbooks. These "myths" constitute exceedingly stubborn roadblocks toward a realistic understanding of modern international commerce and the necessary measures to protect the economic future of the United States.

First Myth: In a Global World, Nations Trade with Each Other

Let us start with a very unfortunate and misleading statement made by Adam Smith (1976, quoted in Culbertson 1989: 93–94): "All commerce that is carried on betwixt any two countries must necessarily be advantageous to both. The very intention of commerce is to exchange your own commodities for others that you think will be more convenient for you. When two men trade between themselves it is undoubtedly for the advantage of both…. The case is exactly the same betwixt any two nations". Whatever the situation may have been in Smith's time, today it is *not nations* that engage in cross-border trade but business firms. Each private deal between contracting corporations will presumably benefit them both, but internationally there is no implication that a trade package is also going to benefit either nation. Certainly, the two parties involved seek their private profits and do not address the question of potential consequences to their own homeland, and neither would they be in a position to give a valid answer to the question were they to raise it. Unlike domestic trade, where socially damaging deals are discouraged by a network of laws and regulations designed to limit third-party effects, "foreign trade, as it were, makes 'an end run around' the laws, regulations, and customs of the nation, since these do not apply to goods produced in other nations" (Culbertson 1989, pp 94, 95). Indeed, outsourcing and re-importation is more often than not motivated by the very opportunity to circumvent such laws and regulations. Yet, in spite of the fact that it is corporations, not governments, that do the trading, textbooks still work with the "England versus Portugal" or "U.S.A versus China" type of trade models when demonstrating that "free" (better "unregulated") cross-border trade is mutually beneficial. Culbertson (1989, p 95) concluded despairingly: "That for 200 years the desirability of unregulated foreign trade has been argued on the basis of the elementary error of treating for-profit private trade as if it were the same thing as barter exchange arranged between the governments on behalf of the two nations is a point that calls for some reflection."

Second Myth: Trade Between Nations Will Tend to Be Balanced

Another telling aspect of the textbook presentations using nations as trading partners is that they implicitly consider only examples in which trade between the nations is in balance. Each country exports something and imports something else of the same aggregate value. Commodities like wine and corn are traded between Portugal and England as if it were barter exchange, a presentation that precludes any possibility of trade deficits. In Culbertson's (1985, p 29) words: "if the trade is in balance, the industries of the high-wage country cannot shift production to low-wage nations and ship the output back home to sell. The assumption that trade between the nations is in balance thus permits evasion of the whole problem of the international shifting of industries and jobs, and of international wage-competition."[9]

Third Myth: Comparative Advantage Governs International Trade

Long before Adam Smith, economists understood quite well that trade and competition work in a manner to equalize wages between regions, such as between relatively high-wage south England and low-wage north England. Even in the case that commerce crossed international borders, David Hume had no problems accepting the implication of his well-known adjustment mechanism by which foreign trade works toward equalizing wage levels internationally (Culbertson 1989, pp 80–82). Adam Smith (1976, p 477), on the other hand, didn't see things the same way: any free trade that induced the dragging down of British wages and living standards would have to be seen as inconsistent with the benevolent workings of an invisible hand. In order to reconcile his vision of a "natural harmony" type of individualism with the effects of the free movement of goods across borders, he had to assert that trade within a country works somehow differently from trade between countries. Smith reasoned that a capitalist would prefer "the support of domestic to that of foreign industry [because] he intends only his own security…" In dealing with foreign folks and institutions, the concern for security trumps the love of gain, a

[9] In the real world, of course, trade deficits are the norm, especially in trade with low-wage countries. The economist's equilibrium position tends to be a very long-run phenomenon, and is reached through a currency adjustment mechanism that has a direct impact on a country's standard of living. For example, a 10% fall of the dollar will decrease U.S. buying power and standard of living proportionately (Culbertson 1989, pp 95, 96).

lucky circumstance that manifests once again the working of a benevolent "invisible hand."

Some half a century later, David Ricardo (1971, quoted in Culbertson 1984, p 233) repeated Smith's claim that international competition, although mutually beneficial, too, works unlike its domestic counterpart. He asserted that "the same rule which regulates the relative value of commodities in one country, does not regulate the relative value of the commodities exchanged between two or more countries." To back up this claim, Ricardo came up with his famous abstract: "principle of comparative advantage." In this model, what matters is not absolute productivity or costs, but relative or "comparative" productivity or cost.[10] However, its operation, Ricardo made clear, is predicated on capital immobility across international borders. Like Smith, he relied on an insecurity of foreign investments, but added also "a natural disinclination which every man has to quit the country of his birth and connections, and entrust himself with all his habits fixed, to a strange government and new laws…" (Ricardo 1951, quoted in Daly and Cobb 1989, p 214). And such a "check" on capital emigration was so crucial that, of the 973 words Ricardo devoted to explaining the law of comparative advantage, half emphasized the importance of factor immobility (Ruffin 2002, pp 733, 734). Under international capital mobility, absolute advantage would govern all trade. Illustrating the point, and by assuming that a country like Portugal could produce not only wine but also cloth cheaper than England, he tells us that "under such circumstances, the wine and the cloth should both be made in Portugal, and therefore that the capital and labor of England employed in making cloth, should be removed to Portugal for that purpose" (Ricardo 1951, quoted in Ruffin 2002, pp 733, 734).

Some 200 years after Smith and Ricardo, massive international capital mobility has become an undisputed fact, thereby seemingly rendering the idea of comparative advantage unpersuasive. Trade theory, too, has evolved since the early 19th century, but it hasn't departed from the Smith/Ricardo point of view in claiming that trade across national boundaries does work differently from trade within a country. Each year, tens of thousands of students are taught that comparative advantage governs international trade, that such an exchange of goods depends on differences in the internal structure of prices of a trading country, and that free trade will not be affected by differences in their absolute level of cost and prices.[11] Therefore, low-wage nations are not going to take our jobs away; neither could free trade exert a strong downward pull on our wage rates and standard of living. In other words, there's nothing to worry about.

Culbertson could not, and would not, remain quiet when confronted with such a dangerous sedative based on counterfactual premises. To him, the bottom line is that in today's world, with the observed amount of capital mobility across borders,

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[10] To this day, Ricardo's principle is seen as a crowning achievement in economic thought. The relative difficulty of the concept is blamed for the fact that it eludes most "beyond the narrow circle of academic economists" (Krugman 1996, p 1). All the whining about low-wage international competition is the result of a lack of understanding and/or appreciation of the principle.

[11] In higher-level textbooks, the student is informed that the underlying assumption for all the graphical exercises and mathematical theorems is "no international mobility of capital." That assumption is generally relaxed in a chapter on "International Political Economy" located toward the end of the book without addressing the earlier theoretical conclusions anew.

Ricardo's famous principle simply lacks relevance. But for Culbertson, to falsify the soothing textbook models one does not even have to insist on the reality and consequences of international capital immobility. As long as there is no requirement that trade has to be in balance, a low-wage nation (Portugal, in Ricardo's famous illustration) could use its cost advantage to undersell English goods in their home market. As a result, "Portuguese capitalists could expand production [of corn] out of profits of their booming [wine] sales… [even without] British capital [having] moved to Portugal." Culbertson (1985, p 29) continues, "After all, the great Japanese industrial expansion in recent decades, which permitted Japanese output to undersell American output on a huge scale, was not based on American capital."

In all likelihood, matters have not changed much in the 20 years since Culbertson (1985, p 30) wrote that "people who take economics courses seem to learn 'the principle of comparative advantage' all too well. Their hard-earned, though false, 'knowledge' makes them unable to see what otherwise would be obvious—that the undercutting of high-wage production by low-wage foreign production is now drastically reshaping the human world." Meanwhile, however, the situation he was worried about has become much more intense. Instead of just Taiwan and Japan, we are now faced with Korea, China, India, Indonesia and Vietnam, all eager to put to use their absolute advantage in order to penetrate the U.S. and European markets.

Fourth Myth: The Productive American Worker

A common objection raised against the idea that low-wage international competition threatens American wage levels is the mistaken notion that U.S. wages are high because of the high productivity of American workers. Culbertson quotes the well-known textbook by Paul Samuelson (Samuelson 1980, quoted in Culbertson 1984, p 179): "High American real wages come from high efficiency, not from tariff protection. Such high wages, the result of productivity, do not handicap us in competing with foreign workers." Such talk seems to imply an assumption that productivity is somehow built into workers, as though it was an intrinsic and unique attribute. Not true, Culbertson (1984, p 15) countered: productivity depends on the value of the product. It is positively affected by demand for those products, including the purchasing power of the working population.[12] Most importantly, the productivity of the American worker depends on the efficiency of the economic system and the character of the foreign-trade system that prevails.

He offers a telling explanation:

> If American auto workers earning $12 an hour become subject to competition from Korean workers earning $1.25 an hour for working in the same kind of factories, the cheap imported cars will undersell the American-produced cars. The price at which American-produced cars can be sold will drop. Then American cars can be sold at a competitive price only by using workers who are getting $1.25 an hour. It is *take wage cuts or lose your jobs*, a familiar refrain of the 1980s.

[12] Technology, of course, is a factor too, but the U.S. has no monopoly on that front.

> If the same production methods are being used in both countries, the "productivity" of the American worker falls, in the simplest case, from $12 an hour to $1.25 an hour. That is what American labor is worth to produce automobiles under the new set of circumstances. Subjecting high-wage workers to competition from low-wage workers can abruptly cut their productivity, the value of what they produce, and require them to accept a drop in wages to hold their jobs. (Culbertson 1985, p 26).

To my knowledge, Culbertson's point that American labor productivity depends on factors that affect the value marginal product of American labor, and consequently also on the extent and nature of unregulated foreign trade, makes for an interesting insight that cries out for more discussion.

Conclusion: Conventional Trade Theory as a Special Case

Like so many basic criticisms of accepted theories, such as Einstein's criticism of Newtonian physics, Culbertson's (1984, p 101) does not claim that free trade theory is altogether inappropriate—he simply relegates it to a special domain. It does have validity in what he calls "a harmonious trade area." Its defining characteristics are the conditions that actually "must be met for the conventional free-trade doctrine to be applicable." In such an area, wage rates and living standards are approximately equal everywhere, there are no significant differences in the rates of population growth among sub-areas, there is general uniformity with regard to standards of worker protection and guardianship of the environment, and there is a similarity in social values concerning the future quality of life and the limits of the market in allocating resources. Generally, such conditions are fulfilled within a mature economy such as in the United States, Japan, Australia, or the nations of Western Europe. Moreover, significant externalities are to a large extent internalized into the costs and prices, while business plays by the same social standards. As a result, the opportunities for degenerative competitive processes are minimized. In such an ideal situation, trade cannot be governed by differences in intra-national levels of wages, incomes, prices, and social standards guiding production, and therefore international commerce is not dependent on absolute advantage or cost. Similarly, trade imbalances between the various regions will tend to be non-existent, or at least very temporary.

The problem, of course, is that contemporary North–South trade is not at all described as such a harmonious trade area: instead, we have huge differences in wages, incomes, population growth, etc. Yet, the doctrine of free trade ends up treating the whole global economy as if it were harmonious in that regard. Even if it were not, comparative advantage comes to the rescue by asserting that the way international trade works does not depend on absolute advantage. Incorrect, says Culbertson: free trade will benefit all countries only in the very special case of trade deficits among the trading partners being for all practical purposes absent. Unfortunately, this won't happen when corporations do the trading with low-wage countries.

A simple illustration by means of a hypothetical example may help clarify matters: suppose that China and the U.S. produce computers and bicycles. China can produce both goods much more cheaply—especially the bicycles built largely with, let us say, prison labor. Theoretically, a balanced exchange between the two countries in these two goods would be in the interest of both nations and therefore theory dictates a trade pattern in which both nations would gain. Practically, on the other hand, U.S. companies like Dell or IBM are not in the least interested in such abstract theory-derived dictates: they, too, will want to produce in low-wage China. Absolute advantage trumps the comparative kind. In such a situation, only when the countries' governments manage trade, can it be balanced and made mutually beneficial. This brings us to the related topic of trade policy.

Culbertson's Proposal of an Alternative Trade Policy

Luckily, the theories of Smith and Ricardo were not the hallmark of subsequent British trade policy. As Culbertson (1989, p 89) observed, "England's trade policy was realistic, tough, and oriented to the interests of England—like today's trade policy of Japan, and other nations. This distinction of literally applying the free-trade doctrine to one's national policy, and of turning over the nation's markets to other nations to exploit for their benefit—this distinction was left for the United States." Countering these mistaken policies and the threat they pose motivated Culbertson's constructive proposals regarding trade policy. He realized, of course, that setting reasonable American trade policy was bound to be a highly complex matter, that a new vision and strategy would require overcoming obstacles of a practical sort. To begin with, there was the institutional block of General Agreement on Trade and Tariffs (today, the World Trade Organization) enshrining unregulated corporate trade across borders. Another roadblock, this time of a linguistic nature, was the way the entire debate about international trade policy was framed: a choice between "free trade" and "protectionism."

The latter constitutes another one of the many myths clouding the issue. In one of his last speeches, in 1994, Culbertson (1994, p 23) complained, "the posing of the regulation of the nation's foreign trade as a choice between either 'free trade' or 'protectionism' is seriously misleading and propagandistic." He explained that "it is a basic technique of propaganda to 'stack the deck' by including only the option being touted and one alternative that is obviously unacceptable, the options that merit serious attention being denied consideration." The words "freedom" and "free" are both loaded and misleading. What is really at stake is deregulation of the measures intended to protect the national interest—before that, the kingdom, and going further back, the tribe. In Western thought, "freedom" became a positive concept in the context of gaining independence from dominant Great Britain, as in political self-control of a nation like the United States. But "free trade" today has the opposite effect. "The 'freedom' of traders of all nations to engage in foreign trade across the boundaries of the United States," writes Culbertson (1994, p 24), "undercuts the political independence and 'freedom' of Americans in far-reaching and ill-understood ways."

When it comes to "protectionism," this negative stereotype implies that those in favor of any form of trade regulation are either ignorant or simply selfish—as if the support of regulation could not be based on impartial, intelligent argument. In short, Culbertson (1994, p 25) decried the long-maintained conceptualization of the issue as "freedom" versus "protection" as "a masterpiece of misrepresentation" that urgently needs to be replaced by a more meaningful label, such as being a choice between unregulated versus regulated international trade. An objective consideration of trade policy requires escaping from powerful stereotypes and emotionally loaded words to ask open-mindedly the question: what degree and form of regulation (or non-regulation) of a nation's foreign trade will serve its interests? Of course, Culbertson had no illusions that a new framework yielding mutually beneficial trade would be an easy task, but he did provide a general outline of what needs to be done.

Above all, we need a system generating balanced trade; only in this manner can we prevent the exportation of jobs and industries to low-wage countries. This implies that, except in cases of trade between nations with very similar laws, regulations, income and social standards (i.e., a harmonious trading area), "foreign trade must be arranged, in effect, as a barter exchange between the trading nations, that is, between the national governments" (Culbertson 1989, p 173). Earlier, Culbertson (1984, p 220) made the point that:

> Arrangements for trade that are negotiated directly between the two governments involved thus would be more balanced, would, as it were, put the cards on the table, and would open up the potential for kinds of mutually advantageous trade deals that could not be worked out at lower levels but require the larger perspective and powers of the national governments.

Ideally, such bilateral agreements would best be negotiated by a newly created Foreign Trade Agency, similar to the Japanese Ministry for Foreign Trade and Industry.[13] Besides hammering out quid pro quo trade packages, including countertrade arrangements, its principal function would be the managing of the nation's import budget through the use of import quotas. A limited number of such commercially valuable licenses could be sold to foreign exporters at market price, and the revenue generated by these sales could then subsidize exports of those industries that are deemed strategic in terms of a forward-looking industrial policy (Culbertson 1986, p 128).

Such are the bare bones of a system that would make the doctrine of comparative advantage relevant again—albeit in an altogether different context. The general direction of his proposal is quite straightforward; the details of implementation and enforcement, on the other hand, are much less clear. Neither can one discern today, two decades later, any political readiness, especially on the part of the educated elite in charge of policy makers, to even consider going down a road anywhere like this. But Culbertson (1984, p 225) was clear on one point: the impediment to realistic action does not seem to be so much a conflict of basic values or solid arguments, as the unrealistic theories of the economic textbooks. "It is not difficult to imagine," he writes, "the United States and the West in the years ahead playing out a script that

[13] In Culbertson's (1989, p 179) words: "What is required is an agency that has the power to act on behalf of the nation, that conscientiously and realistically, avoiding the temptations of graft, ideological delusions, factional rivalries, will serve the interests and preserve the future of the nation."

derives from the unrealistic doctrines of economic theory. Many economists wear blinders that will induce them to continue their crusade against ‘protectionism’ all the way to the sinking of the West.” Getting rid of the ideological delusion of free trade as the road to worldwide affluence, and starting to think realistically and scientifically about trade, was for him of utmost importance in order to avoid “a future that is too dismal to contemplate” (Culbertson 1989, p 212).

Academia’s Reaction to Culbertson’s Work

Given all the attention that Culbertson received in the media, one would expect some sort of response from academic economists; after all, rarely was the profession attacked on an issue of such importance. There seemed to be a promising occasion when Culbertson (1987) was invited to present a paper, “A Realistic International Economics,” at a conference on economic education. He used the opportunity to present, in summary fashion, his case against orthodox trade theory and policy. Two economists were invited to act as respondents: Francis Rushing (1987) and Dennis Weidenaar (1987). Although both were politely critical, neither of them chose to address the very heart of the controversy, like the basic myths discussed above.[14]

To my knowledge, only two brief reviews of Culbertson’s books were published in academic journals. One, in *Population and Development Review* (McNicoll 1986), was largely uncritical, and focused on population growth and migration; the other appeared in *Foreign Affairs* (Diebold 1985), and at only 130 words long, it did not contribute much to any debate. Clearly, judged by a virtual lack of reviews, one has to conclude that the reaction of the mainstream discipline has been nothing more than icy neglect. Perhaps Culbertson’s thoughts are indeed an embarrassment to all economists of proper training, or perhaps there are other reasons.

Whatever the case may be, book reviews are not the only way to assess a professor’s influence (or lack thereof). Another avenue consists of ascertaining whether there have been any academic followers, and if so, checking whether their articulation of Culbertson’s thinking has been given much consideration. As to the first question, the answer is definitely yes, but as far as I know, there are only two such followers, both social economists stressing community, human dignity, and the common good.[15] By far the more influential of the two, and without doubt the main proponent of Culbertson’s message to this day, is Herman Daly, who in 1989 co-authored a book that devoted an entire chapter to Culbertson’s alternative trade

[14] Rushing (1987, p 189) concluded: “Professor Culbertson’s process of making international economics more realistic falls short in one important way. If free trade and comparative advantage are to be abandoned for lack of relevance, what is the substitute framework? What new analytical constructs will supersede the old laissez faire? Can it be so loose a construct as government protection and intervention?”

[15] Interestingly enough, both of them were made aware of Culbertson’s first book through their non-economic co-authors. Both initially resisted the new viewpoint, a way of thinking much in conflict with their academic training; but the cognitive dissonance eventually had to yield to argument grounded in common sense and logic.

theory (Daly and Cobb 1989, ch 11). Above all, Daly focused on the irrelevance of comparative advantage in a world of capital mobility. In the process, he added a most powerful example indicating how textbooks mislead students in teaching the logic of comparative advantage in terms of specialization between individuals:

> A classic example is a lawyer who is a better typist than her secretary. Even though the lawyer has an absolute advantage over the secretary both in knowledge of the law and in typing, she nevertheless finds it advantageous to specialize in law (her comparative advantage) and employ the secretary to do the typing. Since there is no possibility for labor power or any other productive capacity to flow out of the secretary and into the lawyer in response to absolute advantage, the assumption of factor immobility is guaranteed, and the principle of comparative advantage works. But the argument cannot be generalized to nations without the explicit requirement that their productive capacities (factors) not flow across national borders. (Daly and Cobb 1989, p 217).

Daly, a doctoral student under Nicholas Georgescu-Roegen at Vanderbilt University, and a Senior Economist in the Environment Department of the World Bank from 1988 to 1994, now teaches at the University of Maryland. He wastes no time spreading Culbertson's insight on trade by fighting what he calls "recitation[s] of the virtues of comparative advantage from the free trade establishment" (Daly 1999, p 128) by grinding out a large number of well-known books, speeches, and online activity.

The other social economist—none other than yours truly—initially mentioned Culbertson's trade critique in a book published in 1988 (Lutz and Lux 1988, pp 284–88). Unlike Daly, the emphasis there was on the problem of unbalanced trade rather than capital mobility. In part inspired by Daly's work, there followed subsequent (and better) articulations on the topic (most recently in Lutz 1999, pp 199–208).

As to the second question relating to critical discussions of the work of Culbertson's followers, there is unfortunately very little to report. To my knowledge, we lack engaging critiques in print seriously trying to rebut the new thinking.[16] Still, Culbertson's work has not gone totally unnoticed. So, for example, in an oft-cited paper, Robert Prasch (1996) refers to Culbertson in his critique of comparative advantage, particularly the assumptions of "balanced barter-like trade" and capital immobility. Others have also started to question the relevance of trade theory, given the enormous degree of international capital mobility, but they do so without any reference to the pioneering work of Culbertson. The most prominent among these are William Greider (1997), the former supply-sider Paul Craig Roberts (2004), and

[16] To illustrate: three leading social economists were invited to write a review essay on Lutz (1999); only two, Daniel Fusfeld and Steven Pressman, discussed the material on trade. Fusfeld (2001, p 99), while himself agreeing with the general thrust of the argument, comments on the critique of the theory of comparative advantage: "Many readers of this book will agree with [the] critique—except of course, the international trade theorist, who will respond: 'we've heard all this before, and found it unconvincing.'" Pressman (2001, p 111) notes about Ricardo-based free trade theory: "Lutz correctly points out that the argument is based upon some rather unrealistic assumptions, and so the case for free trade may not hold in the free world." But to him it was not clear what trade theory had to do with social economics.

the former Harvard Business professor turned activist, David Korten (1995).[17] Finally, disturbingly noteworthy is a supposedly comprehensive assessment of the free trade paradigm that discusses "new and persistent heresies" without mentioning anything whatsoever related to the Culbertson critique of trade theory (Went 2000).

Conclusion: Culbertson's Standing Challenge

In assessing Culbertson's contributions, it helps to know what he was up against: an entrenched establishment consisting today of some 1500 international trade economists, many sporting pedigrees that suggest notable intellectual descent from the very best university departments.[18] In defending the basic premise that international trade is indeed beneficial, they work in an abstract and unreal world, a mathematical habitat. There, countries with well-defined (in the case of unbalanced trade, even homothetic!) community preference functions do the trading with each other. The structural framework needs to be one of perfect competition and frictionless trade, with no externalities, no increasing returns, or anything else that would interfere with comparative advantage working its magic.

Stepping outside of the "sandbox world," economist Deardorff (2005, pp 22, 23), a representative of orthodoxy, readily admits that "there may be good reasons to doubt that trade in the real world is beneficial, but the presence of frequent instances of distortion and increasing returns suggests that we are ignorant, not necessarily wrong." But he then concludes with a commendable, remarkable, and worthwhile confession: "My own stake in this discussion [of the state of trade theory] would make it *impossible to accept that comparative advantage is a useless concept*" (emphasis added). Reader take note!

The crux of the problem, of course, is that outside of the learned economic models, comparative advantage, an artificial concept rooted in a lack of real knowledge, is being advertised to policy makers as a silver bullet against protectionist inefficiencies and for a stronger economy. Culbertson dared to confront this ideological establishment, showing that comparative advantage is not only useless, but also dangerously destructive. By reasoned argument and a healthy dose of common sense, he established that because corporations, not nations, do the trading, international exchange is driven by absolute cost levels and absolute advantage. To my knowledge, nobody before him had pointed that out, or the very worrisome implications of trade with low-wage, over-populated countries. In a

[17] Roberts' activist critique of comparative advantage based on outsourcing has also captured the imagination and support of New York Senator Chuck Schumer (Schumer and Roberts 2004). Not surprisingly, the resulting publicity soon provoked some responses on the mises.org blog and a brief article by George Mason University economist Donald Boudreaux (2004). There, Boudreaux claims that Roberts simply does not understand comparative advantage. In the present context, it is easy to see that Dr. Boudreaux is barking up the wrong tree. As long as a country produces something, with or without international capital mobility, a ratio demonstrating comparative advantage may be computed, but such a number indicating the public interest will not necessarily govern the trade of a nation. In the case at hand, it is the investor-owned corporation seeking maximum private profits that will follow *absolute* advantage in deciding whether or not to outsource.

[18] See http://www-personal.umich.edu/~alandear/tree/INDEX.HTM, maintained by A.V. Deardorff.

sense, he may have managed to undermine, perhaps even undo, the very rationale for international trade as a separate field in economics.

It is my hope that social economists of all colors will take notice of Culbertson's work, evaluate it critically, and then decide for themselves whether it passes muster, or whether it is just another populist "flat earth theory." In the latter case, many of us would greatly profit in being told exactly where Culbertson blundered, or just how the argument falls flat.

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Mark A. Lutz was born in New York, grew up in Switzerland, and earned his M.A. and Ph.D. degrees in economics at the University of California, Berkeley. He taught at the University of Maine from 1970 till his retirement in 2001. For three decades he has been a member of the Association of Social Economics, serving in various capacities, including as president, and was also privileged to be awarded the Thomas Divine Award. His longtime interests have centered on a more humanistic approach to economics, a viewpoint centered on human wellbeing, which can be traced back to the early 19th century. It's a vision of the economy where there has long been much skepticism about the alleged benefits of unregulated market competition coordinating economic activity within or between nations.